FILED
DEC 31 1997
CLERK

(2)

No. 97-1075

IN THE
Supreme Court of the United States
OCTOBER TERM, 1997

AMERITECH CORPORATION, *et al.*,
Petitioners,
v.
FEDERAL COMMUNICATIONS COMMISSION, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

---

RESPONSE OF MCI TELECOMMUNICATIONS CORPORATION TO CONDITIONAL CROSS-PETITION OF REGIONAL BELL COMPANIES

THOMAS F. O'NEIL III
WILLIAM SINGLE, IV
MCI TELECOMMUNICATIONS CORPORATION
1133 19th Street, N.W.
Washington, D.C. 20036
(202) 736-6412

BRUCE J. ENNIS, JR.*
DONALD B. VERRILLI, JR.
MARK D. SCHNEIDER
ANTHONY C. EPSTEIN
JENNER & BLOCK
601 13th Street, N.W.
Washington, D.C. 20005
(202) 639-6000
Counsel for Respondent MCI Telecommunications Corporation

* Counsel of Record

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

17 pp

QUESTIONS PRESENTED

1. Did the Eighth Circuit correctly apply *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.* and give appropriate deference to a Federal Communications Commission rule that competitors seeking to provide local telephone service may provide service entirely through combinations of unbundled network elements leased from the incumbent local telephone company.

2. Did the Eighth Circuit correctly apply *Chevron* and give appropriate deference to an FCC rule that the hardware and software of the telephone switch which make functions like "call forwarding" and "caller ID" possible are "features" and "functions" of the switch within the statutory definition of "network elements" that must be provided to competitors on an unbundled basis.

RULE 29.6 STATEMENT

Pursuant to Supreme Court Rule 29.6, respondent MCI states as follows:

MCI Telecommunications Corporation is a wholly-owned subsidiary of MCI Communications Corporation. MCI has the following non-wholly owned subsidiaries: General Communications, Inc.; IFP Holdings, Inc.; ICS Communications, Inc.; Digital Network Television, Inc.; Genesys Telecommunications, Inc.; Inflight Phone Corp.; Multimedia Medical Systems, Inc.; News T Investments, Inc.; News Triangle Finance, Inc.; Pioneer Holding L.L.C.; Portugal Telecom; and Security Technologies, Inc.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
RULE 29.6 STATEMENT	ii
TABLE OF AUTHORITIES	iv
STATEMENT OF THE CASE	1
ARGUMENT	4
I. THE COURT SHOULD GRANT CROSS-PETITIONERS' FIRST QUESTION PRESENTED AND CONSIDER IT ALONG WITH THE RELATED QUESTIONS PRESENTED IN THE PREVIOUS CERTIORARI PETITIONS	4
II. THE COURT OF APPEALS DECISION TO DEFER TO THE FCC'S JUDGMENT THAT "VERTICAL FEATURES" ARE NETWORK ELEMENTS WAS CORRECT AND RAISES NO QUESTION MERITING PLENARY CONSIDERATION	8
CONCLUSION	12

TABLE OF AUTHORITIES

CASES	Page
Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984)	8
LEGISLATIVE MATERIALS	
47 U.S.C. § 153(29)	9
47 U.S.C. § 251(c)(3)	*passim*
47 U.S.C. § 251(d)(1)	8
47 U.S.C. § 254	7, 8
47 C.F.R. § 51.307(a)	2, 3
47 C.F.R. § 51.307(c)	2, 9
47 C.F.R. § 51.315(b)	*passim*
47 C.F.R. § 51.319(c)(1)(C)	2, 9
H.R. Conf. Rep. No. 104-458, 104th Cong., 2d Sess. (Jan. 31, 1996)	7
In re Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, First Report and Order, CC Docket No. 96-98, FCC 96-325 (Aug. 8, 1996)	10, 11

IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

No. 97-1075

AMERITECH CORPORATION, *et al.*,
Petitioners,

v.

FEDERAL COMMUNICATIONS COMMISSION, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

---

RESPONSE OF MCI TELECOMMUNICATIONS CORPORATION TO CONDITIONAL CROSS-PETITION OF REGIONAL BELL COMPANIES

MCI Telecommunications Corporation ("MCI") acquiesces to a grant of certiorari on the first question presented in the above-captioned petition, conditioned upon the granting the related question in MCI's petition for certiorari (No. 97-829), and opposes certiorari on the second question presented.

STATEMENT OF THE CASE

The relevant facts are for the most part set out in the original petitions for certiorari to which this conditional cross-petition relates, and will not be repeated here.[1] In

[1] Nos. 97-826, 97-829, 97-830, 97-831.

their cross-petition, the Regional Bell Operating Companies ("RBOCs"), which are the local telephone monopolies that were once part of the Bell System, conditionally challenge the Eighth Circuit's decision to uphold two Federal Communication Commission ("FCC") regulations implementing provisions of the Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) ("1996 Act" or "Act"). In particular the RBOCs challenge the Eighth Circuit's decision to uphold: (1) 47 C.F.R. § 51.307(a), which allows a potential competitor to lease network elements from the incumbent local exchange carrier ("incumbent LEC"), regardless of whether the competitor employs any facilities of its own; and (2) 47 C.F.R. §§ 51.307(c) and 51.319(c)(1)(C), which define features such as "call waiting" and "caller ID" to be "features and functionalities" of the switching element that can be leased by competitors when they lease switching as an unbundled network element pursuant to 47 U.S.C. § 251(c)(3).

On the first question presented in the cross-petition, the Eighth Circuit concluded that the "plain language of subsection 251(c)(3) indicates that a requesting carrier may achieve the capability to provide telecommunications services completely through access to the unbundled elements of an incumbent LEC's network." Pet. App. 55a. The court accordingly rejected the incumbent LECs' argument that new entrants should be prevented from leasing unbundled network elements unless they also employed their own facilities and equipment to provide local service. In this regard, the Eighth Circuit expressly rejected the incumbent LECs' argument that by "allowing a competing carrier to obtain the ability to obtain finished telecommunications services entirely through unbundled elements at the less expensive cost based rate [which the 1996 Act dictates for such elements], the FCC enables competing carriers to circumvent the more expensive wholesale rates that the Act requires for telecommunications services."

Pet. App. 54a. The Eighth Circuit also expressly rejected the incumbent LECs' argument that "by being able to obtain the ability to provide services at cost under Subsection 251(c)(3), competing carriers will be able to capture many of the incumbent LECs' customers to whom the incumbent LECs are expected to charge high prices for certain services to offset the low prices incumbent LECs are required to charge other customers in order to promote universal service." *Id.* The Eighth Circuit noted that even if the FCC's reading of § 251(c)(3) produced such marketplace effects, "we believe this result is entirely consistent with the Act's purpose to promote competition in local phone markets," and that "section 254 of the Act . . . reveals Congress's intent to overhaul the current system of support for universal service, which is based on the incumbent LECs' supracompetitive prices for certain service," with a rational and competitively neutral explicit subsidy program. *Id.* at 57 n.34.

Although the Eighth Circuit rejected the incumbent LECs' challenge to § 51.307(a) of the FCC's rule, on rehearing the court invalidated § 51.315(b) of those rules—which prohibited incumbent LECs from breaking apart existing combinations of network elements ordered by new entrants—on the ground that "[t]o permit such an acquisition of already combined elements at cost based rates . . . would obliterate the careful distinctions Congress has drawn . . . between access to unbundled network elements on the one hand and the purchase at wholesale rates of an incumbent's telecommunications services for resale." Pet. App. 71a. In reaching this result, also urged by the incumbent LECs to preserve universal service, the Eighth Circuit did not, however, revisit its earlier conclusion that the very purpose of the 1996 Act was to allow new entrants to drive down supracompetitive rates that allegedly funded universal service in the past, and to replace the old, anticompetitive system of implicit subsidies with a

new procompetitive system of explicit universal service subsidies.

On the second question presented in the cross-petition, the Eighth Circuit concluded that vertical features such as caller ID and call waiting "are provided through the switching hardware and software that are also used to transmit calls across phone lines," and are thus plainly within the Act's definition of "network element." Pet. App. 44a.

ARGUMENT

I. THE COURT SHOULD GRANT CROSS-PETITIONERS' FIRST QUESTION PRESENTED AND CONSIDER IT ALONG WITH THE RELATED QUESTIONS PRESENTED IN THE PREVIOUS CERTIORARI PETITIONS.

1. The first question presented in the RBOC cross-petition confirms the urgent need for review of the Eighth Circuit's decision to invalidate § 51.315(b) of the FCC's rules. By invalidating § 51.315(b), the Eighth Circuit allowed the incumbent monopolists to saddle new entrants such as MCI with discriminatory costs that would make competitive entry through the use of combinations of unbundled elements impossible in wide segments of the market. The United States, as well as MCI, AT&T and many other competitors in local telephone markets sought certiorari on this question because the Eighth Circuit's ruling is having a devastating effect on the Congressional objective of achieving competition in local markets as quickly as possible. In opposing certiorari, the RBOCs cavalierly dismissed the Eighth Circuit's invalidation of § 51.315(b) as a "second level," "tag along" issue unworthy of this Court's attention. Brief in Opposition of the Regional Bell Operating Companies 2, 21. Now, in a remarkable about-face, the RBOCs insist that the lower court's invalidation of § 51.315(b) enforced a "critical statutory distinction" (RBOC Cross-Pet. 22), that was "crucial to the court of appeals' decision" (*id.* at 13) because it

blocked "a more favorable path for potential competitors" (*id.* at 22) that would, in the RBOCs' view, threaten key objectives of national telecommunications policy.

Indeed, cross-petitioners insist that the Eighth Circuit's decision to invalidate § 51.315(b) is so critical that if this Court is to review it, the Court must also review the Eighth Circuit's related decision upholding the right of new entrants to compete entirely through use of unbundled elements. The RBOC's position is that the Eighth Circuit was required *either* to invalidate § 51.315(b) *or* to make clear that the Act did not allow new entrants to compete in local markets exclusively through combinations of network elements. That is so, the RBOCs argue, because unless the price to new entrants of using network elements is artificially inflated well above their cost (so that as a practical matter elements cannot be used in combination) or the use of elements in combination is forbidden altogether, new entrants will be able to price retail services at levels that threaten the supracompetitive profits the incumbents now earn from urban and business customers. This, the RBOCs then claim, would threaten their ability to provide affordable service to other classes of customers (chiefly rural customers who live where it is more expensive to provide service) whose rates are now purportedly subsidized by the supracompetitive profits.

In sum, both sides to this dispute now agree that the Eighth Circuit's invalidation of § 51.315(b) was critically important—MCI because its invalidation blocked the use of unbundled network elements as a competitive entry strategy, and the RBOCs because its invalidation preserves supracompetitive profits allegedly needed to support universal service. This Court should therefore grant certiorari to review that aspect of the Eighth Circuit's decision.

2. MCI agrees that certiorari also should be granted on the first question presented in the RBOC cross-petition because that question is closely related to the first question

presented in MCI's petition for certiorari. In addressing MCI's claim that the Eighth Circuit impermissibly relied on faulty policy assumptions in striking down § 51.315(b), the incumbent LECs will undoubtedly defend the judgment below on the ground that the artificial costs imposed on new entrants as a result of the Eighth Circuit's decision are necessary to protect universal service subsidies. The RBOC cross-petition is correct that any such defense necessarily implicates the Eighth Circuit's related decision that § 251(c)(3) permits new entrants to rely exclusively on unbundled elements to compete in local markets. Thus, the proper course is to consider both questions together.

3. Though we acquiesce in review of cross petitioners' first question presented, that is not because of any doubt that the plain text of the Act permits new entrants such as MCI to provide service entirely through the use of unbundled elements. As the Eighth Circuit held, §251(c)(3) requires incumbent LECs to make unbundled network elements available to "any" telecommunications carrier, not merely those who already have built parts of their network.

The problem with the Eighth Circuit's ruling was not its effectuation of the statutory command that new entrants be permitted to rely entirely on unbundled elements to provide service. Rather, the Eighth Circuit erred when it invalidated § 51.315(b) for the express purpose of raising the cost to new entrants seeking to use combinations of unbundled elements. The Eighth Circuit thought it necessary to impose such artificial cost to preserve "the careful distinctions Congress has drawn" between using unbundled elements and reselling local service (Pet. App. 71a) —in other words, to increase the cost of network elements so that they could not be a less expensive entry vehicle than resale.

As demonstrated in MCI's petition for certiorari, the Eighth Circuit was acting beyond both its authority and

its expertise in rendering such a ruling. Having properly concluded that the plain terms of the Act allow new entrants to compete exclusively by using combinations of network elements, the Eighth Circuit simply had no basis in the Act for seeking to make that mode of competing more expensive than resale. Its policy determination that one mode of entry needed to be burdened with otherwise unnecessary costs so that another mode of entry would become relatively more attractive is quintessentially a matter committed to Congress, and if necessary, agency discretion, and the court had no business rejecting both Congress' and the FCC's judgment that the two modes of entry were sufficiently distinct to make the Eighth Circuit's policy choice both unnecessary and unwise.

The RBOCs nevertheless seek to justify this decision as necessary to protect implicit universal service subsidies. But that justification is utterly irreconcilable with the text, structure and purposes of the 1996 Act. The fundamental purpose of the 1996 Act is to promote local competition and to *eliminate* these very implicit universal service subsidies that the monopolists claimed justified their supra-competitive profits. Congress believed that the public would be better served by a new regime in which competition drove local telephone prices down to competitive levels, and any subsidies necessary to assure universal service would be explicit. In particular, it determined that the prior system of hidden subsidies deterred competition and allowed incumbent LECs to shield grossly inflated profits from meaningful regulatory scrutiny. Thus, in § 254 of the 1996 Act (a provision nowhere mentioned in the cross-petition), Congress eliminated the historic system of implicit universal service subsidies.[2] Accordingly, it directed the creation of explicit, competitively neutral

[2] The Conference Report expressly stated that "any [universal service] support mechanisms . . . should be explicit, rather than implicit as many support systems are today." H.R. Conf. Rep. No. 104-458, 104th Cong., 2d Sess. at 131 (Jan. 31, 1996).

federal and state funding mechanisms designed to ensure affordable local service for all. That mechanism is scheduled to be in place by January 1, 1999. The Eighth Circuit recognized all of this, Pet. App. 57a, n.34, rendering all the more inexplicable its decision to invalidate § 51.315(b).

The incumbent LECs' complaint, then, in the end must reduce to one of timing: if new entrants can rely on unbundled elements to enter local markets *now*, the RBOCs contend, they will be able to compete away the incumbents' supracompetitive profits before these new funding mechanisms are in place. But Congress expressly dictated the timing; its choice is reflected in the fact that it required to the FCC to complete its local competition regulations, including regulations governing competition through unbundled network elements, within six months, 47 U.S.C. § 251(d)(1), while giving the FCC eighteen months to complete universal service reform. *Id.* § 254(a)(1).

In sum, the RBOCs' policy argument based on the need to preserve monopoly profits allegedly to fund implicit subsidies is directly in the teeth of the express policy of the 1996 Act.

II. THE COURT OF APPEALS DECISION TO DEFER TO THE FCC'S JUDGMENT THAT "VERTICAL FEATURES" ARE NETWORK ELEMENTS WAS CORRECT AND RAISES NO QUESTION MERITING PLENARY CONSIDERATION.

Cross-petitioner's second question concerns the Eighth Circuit's straightforward application of *Chevron U.S.A. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), and is neither independently worthy of review, nor sufficiently related to the important questions raised in the original certiorari petitions to warrant review for that reason.

"Vertical features" of a telephone switch are hardware and software that enable the switch to provide added serv-

ices such as "call forwarding" and "caller ID." The second question takes issue with the Eighth Circuit's decision deferring to the FCC's judgment that such vertical features on the incumbent LEC's switches are "features, functions, and capabilities" of the switch, 47 U.S.C. § 153(29), that competitors therefore have the right to lease at cost-based rates. *See* 47 C.F.R. §§ 51.307(c); 51.319(c)(1)(C). Both the FCC and the Eighth Circuit found this result compelled by the plain meaning of the statutory text.

The Act defines "network element" to mean

> a facility or equipment used in the provision of a telecommunications service. Such term also includes features, functions, and capabilities that are provided by means of such facility or equipment, including . . . databases, signaling systems, and information . . . used in the transmission, routing, or other provision of a telecommunications service.

47 U.S.C. § 153(29). There is no dispute that switching is a "network element" that can be leased by competitors, just as there is no question that the basic software embedded in the switch needed to route any telephone call is part of what is leased when companies lease the switch. And there is no dispute that the switching software that make *added* services such as "caller ID" possible also include "databases, signaling systems and information . . . used in the transmission, routing or other provision of a telecommunications service." *Id.* In this regard, the software that make added services possible are in relevant respects no different from the software that make basic switching functions possible.

Given all this, and relying on this statutory definition, the FCC determined that vertical features are every bit as available for lease as a part of unbundled switching as is the basic switching function, concluding that "[v]ertical switching features, such as call waiting, are provided through operation of hardware and software comprising

the 'facility' that is the switch, and thus are 'features' and 'functions' of the switch."[3] The Eighth Circuit reviewed the FCC's Order and the statute and found that vertical features "satisfy the definition of 'network element;' consequently they are subject to the unbundling requirements of subsection 251(c)(3)." Pet. App. 45a.[4] It agreed with the FCC that the RBOC's argument to the contrary "would allow the incumbent LECs to evade a substantial portion of their unbundling obligation." Pet. App. 44a-45a. It therefore concluded that the FCC's rules were entitled to deference under *Chevron*.

The plain meaning of the relevant provisions of the Act virtually compelled the FCC and the Eighth Circuit to reject the RBOCs' efforts to require that vertical features be treated differently than other capabilities of a switch. Quite simply, vertical features are "features, functions and capabilities" of a switch. *Local Competition Order* ¶ 413. Cross-petitioners nevertheless insist that their own policy priorities must trump such plain meaning analysis, and that competitors should pay supracompetitive prices if they wish to use the leased switch's vertical features. They reason that because these vertical features make possible telecommunications services than can be purchased directly by consumers, the features are properly considered "services," and that "services" cannot be at the same time also be "elements," regardless of the statutory definition.

But nothing in the Act says, or even suggests, that "services" and "elements" must be mutually exclusive cate-

---

[3] *First Report and Order, In re Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-98, FCC 96-325, ¶ 423 (Aug. 8, 1996) (*"Local Competition Order"*), reprinted at RBOC Cross-Pet. App. 12a.

[4] Strictly speaking, the FCC did not find that vertical features themselves are independent "network elements," but rather that they are "features, functions and capabilities that are provided by means of" the switching element. *Local Competition Order*, ¶¶ 412-414.

gories. In the RBOC's view, the Eighth Circuit nevertheless committed error in refusing to "consider[] the practical consequences of the FCC's approach." RBOC Cross-Pet. 23. Those consequences, in cross-petitioners' view, are that competitors will be able to offer their customers vertical services leased from cross-petitioners at a lower retail price than the inflated prices cross-petitioners are currently offering. And, repeating the theme of their cross-petition, the RBOCs insist that if competitors can compete effectively by offering local telephone services at cost-based rates, that will deny the monopolists the profits they claim to need to support implicit universal service subsidies. *Id.*

For the reasons we have just discussed, that policy rationale is insupportable. Even apart from cross-petitioners' mistaken assumptions about universal service, as the FCC observed in rejecting this argument, it cannot be that every element that could be characterized as a "service" for that reason is unavailable for lease. *Local Competition Order*, ¶263. Switching, operator services, and lines that run from the switch to the business location have all been or could easily be offered as "services" available to retail customers. If none of these elements as a result could be considered "network elements," the statutory provisions that allow for competitive service through combinations of unbundled network elements would be a dead letter. Although cross-petitioners suggest that it would have been better policy had Congress *not* required the unbundling of their networks, *see* RBOC Cross-Pet. 5, n.3, their suggestion that the Eighth Circuit erred in not carrying out this policy preference is frivolous.

Most of all, on this issue at least the Eighth Circuit correctly understood that under *Chevron* it was *not* its role to "consider[] the practical consequences of the FCC's approach," RBOC Cross-Pet. 23, when that approach is virtually compelled by the plain words of the statute. Cross-petitioners' invitation to this Court to take on this role should be dismissed out of hand.

Neither is this question fairly encompassed within the combination issues that are the subject of the original petitions and the first question presented in this cross-petition. At issue here is the narrow question of which features of the switch should be available to competitors for lease as network elements. This question therefore does not raise the larger questions raised in the initial petitions or the first question of the cross-petition, concerning competitors' ability to compete through the use of combinations of unbundled network elements. There is therefore no reason to grant plenary review of this second question in order to "ensure that the full scope of the lower court's unbundling decision is properly before it." RBOC Cross-Pet. 13-14.

CONCLUSION

The Court should grant the conditional cross-petition's first question presented at the same time it grants the related questions presented in the petitions filed by the United States, MCI, and AT&T *et al.* The Court should deny the petition on the second question presented.

Respectfully submitted,

THOMAS F. O'NEIL III
WILLIAM SINGLE, IV
MCI TELECOMMUNICATIONS CORPORATION
1133 19th Street, N.W.
Washington, D.C. 20036
(202) 736-6412

BRUCE J. ENNIS, JR.*
DONALD B. VERRILLI, JR.
MARK D. SCHNEIDER
ANTHONY C. EPSTEIN
JENNER & BLOCK
601 13th Street, N.W.
Washington, D.C. 20005
(202) 639-6000
Counsel for Respondent MCI Telecommunications Corporation

* Counsel of Record